

IRS News Release

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IRS Gives Investors the Benefit of Pending Technical Corrections on Qualified Dividends

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WASHINGTON —The Treasury Department and the Internal Revenue Service have agreed to make certain provisions of the Tax Technical Corrections Act of 2003 related to dividend income available to taxpayers in advance of its passage. These provisions will be of particular interest to certain mutual fund shareholders and other investors who are completing their 2003 tax returns.

The Chairmen and Ranking Members of both the House Ways and Means Committee and the Senate Finance Committee have advised the Treasury Department and the IRS that they plan to enact legislation to make the technical corrections in Section 2 of the Act effective for dividends received beginning January 1, 2003. To reduce the burden of requiring amended dividend statements to investors, who might then have to amend their tax returns, the Treasury Department and the IRS have agreed to let all taxpayers apply the technical corrections in Section 2 of the Act as if the legislation were already enacted.

Some mutual funds that received payments from partnerships have delayed issuing Forms 1099-DIV to shareholders while awaiting enactment of these corrections. The Act will allow partnerships, S corporations, estates and revocable trusts treated as part of an estate on a fiscal year that began in 2002 to pass through dividends received in 2003 to their partners, shareholders and beneficiaries as dividends qualifying for the lower tax rates, to the extent that the dividends are otherwise qualified.

The Act will also change the holding period test for qualified dividends. To qualify for the lower tax rates, the taxpayer must now hold the dividend-paying stock for at least 61 days during the 121-day period (instead of the current 120-day period) beginning 60 days before the ex-dividend date – the first date that the buyer will not be entitled to receive that dividend.

A stock bought on the last day before the ex-dividend date (the latest purchase date for collecting a dividend) can still meet the holding period test for that dividend, since there are 61 days left in the 121-day period. A stock sold on the ex-dividend date (the earliest

selling date after entitlement to a dividend) can also meet the test, since that is the 61st day in the period. So if a taxpayer holds a stock for at least 61 continuous days, the holding period test will be met for any dividend received, unless the risk of loss was diminished.

A similar holding period exists for preferred stock dividends attributable to a period exceeding 366 days. This holding period is at least 91 days during a 181-day period beginning 90 days before the ex-dividend date.

Mutual funds, other regulated investment companies, and real estate investment trusts that pass through dividend income to their shareholders must meet the holding period test for the dividend-paying stocks that they hold in order for corresponding amounts that they pay out to be reported as qualified dividends on Form 1099-DIV. Investors must then meet the test relative to the shares that they hold directly, from which they received the qualified dividends that were reported to them.

The IRS expects to post revised versions of three publications and the instructions for various forms related to dividend reporting – for payors and investors – to its Web site at www.irs.gov later this month. The IRS will not reprint the already-printed versions of these materials to reflect the pending legislation. The affected materials are:

- Pub. 17, Your Federal Income Tax (For Individuals), chapter 9
- Pub. 553, Highlights of 2003 Tax Changes
- Pub. 564, Mutual Fund Distributions

Instructions for:

- Forms 1040 and 1040A, U.S. Individual Income Tax Return, line 9b
- Form 1040NR, U.S. Nonresident Alien Income Tax Return, line 10b
- Form 1041, U.S. Income Tax Return for Estates and Trusts, line 2b
- Form 1065, U.S. Return of Partnership Income, Schedules K and K-1, line 4b(1)
- Form 1065-B, U.S. Return of Income For Electing Large Partnerships, lines 2a through 2c in Part II
- Form 1099-DIV, Dividends and Distributions, line 1b, for issuers only (see also page DIV-1)
- Form 1120S, U.S. Income Tax Return for an S Corporation, Schedules K and K-1, line 4(b)(1)
- Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships, Schedules K and K-1, line 4b(1)